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IN THE

Supreme Court of the United States

October Term—1976

No. 76-463

JOEL H. STERNS, Trustee in Bankruptcy for Callahan Motors, Inc.,

Petitioner,

vs.

PRINCETON BANK AND TRUST COMPANY,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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TABLE OF CONTENTS

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Petitioner, Joel H. Sterns, Trustee in Bankruptcy for Callahan Motors, Inc., respectfully prays that a Writ of Certiorari issue to review the Judgment of the United States Court of Appeals for the Third Circuit originally entered in this proceeding on July 8, 1976. Petition for Rehearing filed by petitioner was denied on August 18, 1976.

Opinion Below

The Opinion of the United States Court of Appeals for the Third Circuit is attached hereto as part of the Appendix and is as yet unreported. The Opinion of the United States District Court for the District of New Jersey is attached hereto as part of the Appendix and is reported at 396 F. Supp. 785 (D.N.J., 1975). The Opinion of the Bankruptcy Court is attached hereto as part of the Appendix and is unreported.

Jurisdiction

The Judgment of the United States Court of Appeals for the Third Circuit was entered on July 8, 1976, and the Petition for Rehearing was denied on August 18, 1976. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

Question Presented

Whether the decision of the United States Court of Appeals for the Third Circuit, by subjecting the Trustee in Bankruptcy to equitable considerations, has defeated his rights and powers under Section 70(c) of the Bankruptcy Act (11 U.S.C. 110(c)), and as such has severely affected the proper administration of the Bankruptcy Act contrary to the terms and provisions thereof, and the intention of Congress?

Statutes Involved

11 U.S.C. 110(c) provides:

> (c) The trustee may have the benefit of all defenses available to the bankrupt as against third persons, including statutes of limitation, statutes of frauds, usury, and other personal defenses; and a waiver of any such defense by the bankrupt after bankruptcy shall not bind the trustee. The trustee shall have as of the date of bankruptcy the rights and powers of: (1) a creditor who obtained a judgment against the bankrupt upon the date of bankruptcy, whether or not such a creditor exists, (2) a creditor who upon the date of bankruptcy obtained an execution returned unsatisfied against the bankrupt, whether or not such a creditor exists, and (3) a creditor who upon the date of bankruptcy obtained a lien by legal or equitable proceedings upon all property, whether or not coming into possession or control of the court, upon which a creditor of the bankrupt upon a simple contract could have obtained such a lien, whether or not such a creditor exists. If a transfer is valid in part against creditors whose rights and powers are conferred upon the trustee under this subdivision, it shall be valid to a like extent against the trustee. In cases where repugnancy or inconsistency exists with reference to the rights and powers in this subdivision conferred, the trustee may elect which rights and powers to exercise with reference to a particular party, a particular remedy, or a particular transaction, without prejudice to his right to maintain a different position with reference to a different party, a different remedy, or a different transaction.

N.J.S.A. 12A:9-403 (2) and (3) provides:

> (2) A filed financing statement which states a maturity date of the obligation secured of 5 years or less is effective until such maturity date and there-

after for a period of 60 days. Any other filed financing statement is effective for a period of 5 years from the date of filing. The effectiveness of a filed finacing statement lapses on the expiration of such 60-day period after a stated maturity date or on the expiration of such 5-year period, as the case may be, unless a continuation statement is filed prior to the lapse. Upon such lapse the security interest becomes unperfected. A filed financing statement which states that the obligation secured is payable on demand is effective for 5 years from the date of filing.

(3) A continuation statement may be filed by the secured party (i) within 6 months before and 60 days after a stated maturity date of 5 years or less, and (ii) otherwise within 6 months prior to the expiration of the 5-year period specified in subsection (2). Any such continuation statement must be signed by the secured party, identify the original statement by the file number and state that the original statement is still effective. Upon timely filing of the continuation statement, the effectiveness of the original statement is continued for 5 years after the last date to which the filing was effective whereupon it lapses in the same manner as provided in subsection (2) unless another continuation statement is filed prior to such lapse. Succeeding continuation statements may be filed in the same manner to continue the effectiveness of the original statement.

Statement of the Case

On March 5, 1965, Princeton Bank and Trust Company filed a Financing Statement with the Secretary of State

of New Jersey showing the Debtor as Cregar Motors, Inc. (predecessor of Callahan Motors) and which purported to cover all new and used motor vehicles and the proceeds of sales thereof. On or about December 29, 1967, Princeton Bank and Trust Company filed a continuation statement and change of Debtor's address with the Office of the Secretary of State of New Jersey, allegedly pursuant to N.J.S.A. 12A:9-403. However, the continuation statement was filed twenty-one (21) months before the maturity date of original financing statement. The statute states that the continuation statement may be filed within six months before the maturity date. N.J.S.A. 12A:9-403(3).

Although the Secretary of State accepted and filed the continuation statement and change of address along with the appropriate fees, on December 29, 1967, it never informed Princeton Bank and Trust Company that the filing of the continuation statement would be deemed ineffective because it was premature and that no record would be made thereof. The Secretary of State eventually removed all the records one year after the original maturity date of the original financing statement—March 5, 1970.

On February 22, 1973, the Debtor, Callahan Motors, Inc., having changed its corporate name from Cregar Motors, filed a Petition for Arrangement under Chapter XI of the Bankruptcy Act. As a result of the filing, an Order was entered appointing the Petitioner, Joel H. Sterns, Esq., as Receiver. On December 30, 1974, Callahan Motors, Inc. was adjudicated a Bankrupt.

On March 14, 1973, Princeton Bank and Trust Company filed a Notice of Motion in the Bankruptcy Court to Reclaim Property in which it was alleged that automobiles in possession of the Debtor were secured in favor of the bank.

However, as of the date of the filing of the Petition under Chapter XI of the Bankruptcy Act, a search by the office of the Secretary of State of New Jersey disclosed no financing or continuation statements on file with respect to the claimed security interest of Princeton Bank and Trust Company in the new and used automobiles then in the possession of Callahan Motors and in the proceeds from the sale of any previously sold vehicles.

The Honorable Amel Stark, Bankruptcy Judge, held that since N.J.S.A. 12A:9-403(3) sets the time period for filing a continuation statement to be six months before the expiration of the original financing statement. The filing by the bank twenty-one (21) months before such date was premature and thus failed to give the bank a continued perfected security interest in the collateral of the Debtor Callaghan Motors.

Judge Stark noted in his Opinion that "... it has been well settled for more than a century that filing requirements of this type will be strictly enforced." (37a) He went on to state (40a):

> "Having failed to perfect its security interest, Applicant bank has no priority over the Receiver and the creditors represented by the Receiver."

The United States District Court for the District of New Jersey affirmed the decision of the Bankruptcy Court. Judge Clarkson S. Fisher stated that (23a):

> "... it cannot be thought that in applying a liberal construction of the UCC, clear and unambiguous language should be overlooked to defeat requirements of timely filing imposed by 12A:9-403(3) ...
>
> The Court finds, therefore, that N.J.S.A. 12A:9-403(3) presents in clear and unambiguous language, the standard which must be followed in filing a Continuation Statement. There exists no ambiguity in the word 'may' as such word refers to whether or not a Continuation Statement is, in fact, filed. It has no reference to the prescribed six-month period in which to file." (24a)

Judge Fisher also held that though the Office of the Secretary of State accepted the continuation statement, such acceptance was the result of the Bank's erroneous premature filing.

The United States Court of Appeals for the Third Circuit reversed. The reversal however was not based upon an interpretation of N.J.S.A. 12A:9-403(3), but upon general equitable considerations. The Opinion by Judge Hunter stated (7a):

> "While we find much of the Appellee's argument for a mandatory construction persuasive, we do not find it necessary to decide the question...
>
> In sum, we decline to decide whether under New Jersey law, a Continuation Statement is timely if filed more than six months before the expiration of a Financing Statement or should always be deemed timely if accepted by the filing officer; we hold only that on these particular facts, a resolution of these questions so as to bar appellant's motion to reclaim would be inconsistent with the equitable character of bankruptcy proceeding." (11a)

Petitioner seeks a review of the decision of the Third Circuit Court of Appeals.

Reasons for Granting the Writ

The Writ of Certiorari to the Third Circuit Court of Appeals should be granted by this Honorable Court in order to resolve the conflict between the decision of the Third Circuit in this matter and the clear intent and language of Section 70(c) (11 U.S.C. 110(c)), of the Bankruptcy Act and the cases which have construed that Section.

It has been held that pursuant to Section 70(c), the Trustee attains the status of an ideal lien creditor as of the date of the Petition in Bankruptcy (or Arrangement). The Trustee, pursuant to Section 70(c) is without notice as to any unperfected liens, and that accordingly he takes priority on behalf of all the creditors, over any unperfected security interest a creditor may have in the Bankrupt's property. *Sequoia Machinery Co.* v. *Jarrett,* 410 F. 2d 1116 (9th Cir., 1969). In *Sequoia, supra,* the Ninth Circuit Court of Appeals held that where a creditor had filed a Financing Statement *only* in the Office of the Secretary of State and not in the two Counties where the equipment was being used, the alleged secured creditor's interest was deemed to be unperfected as against the Sec. 70(c) powers of the Trustee in Bankruptcy. See also *United States* v. *Spears,* 382 U. S. 266 (1965); *In Re P. S. Products Corp.,* 435 F. 2d 781 (2nd Cir., 1970); *In Re Dennis Mitchell Industries, Inc.,* 419 F. 2nd 349 (3rd Cir. 1969); *In re Leckie Freeborn Coal Co.,* 405 F. 2d 1043 (6th Cir. 1969); *Carroll* v. *Holliman,* 336 F.2nd 425 (10th Circuit 1964) Cert. Den. 380 U.S. 907 (1965); *In Re Freeman,* 294 F.2d 126 (3rd Cir. 1961); *In Re Parkway Knitting Mills, Inc.,* 119 F. 2d 605 (2nd Cir. 1941); which stand for the proposition that a Trustee in Bankruptcy, under Sec. 70(c)

of the Act, takes priority over and his rights are superior to that of a creditor with an unperfected security interest. The leading treatise in the bankruptcy area is also in accord with the above position. 4A *Colliers on Bankruptcy,* 14th Ed. Sec. 70.53 at p. 636.

> "As demonstrated previously, the Trustee is accorded an 'ideal' status—he is the 'perfect' creditor who has complied with all requirements necessary under the applicable law for a lien by legal or equitable process. He has such status irrespective of whether there are actually any creditors in existence. *He acquires the status from the Act, not from the creditors of the estate.* (Emphasis added) 4A *Colliers on Bankruptcy,* (14th Ed.) Sec. 70.53 at p. 636.

The decision by the Third Circuit in the instant case upholding the alleged secured interest of Respondent, Princeton as against the Receiver, is in conflict with the above cited decisions in other Circuits as well as decisions within the Third Circuit. See *In Re Dennis Mitchell Industries, Inc., supra,* where it was held that a creditor claiming interest must file where the property is located, notwithstanding that the creditor is misled by the Debtor.

> "Both under Sec. 70(c) of the Bankruptcy Act and under Sec. 9-301(3) of the Uniform Commercial Code the Trustee has the status of an ideal lien creditor. Under the Code section the Trustee can be affected with 'knowledge' if it is shown that every creditor of the Bankrupt had such knowledge, which has not been shown here. Under Sec. 70(c) of the Bankruptcy Act, however, the Trustee may have the status of an ideal lien creditor even if all the creditors do in fact have actual knowledge." 419 F. 2d 349, 354.

This conflict between the Circuits is also demonstrated by the following statement from *In Re Parkway Knitting Mills, supra,* a Second Circuit decision:

> "Despite the Appellant's argument to the contrary, there can be no doubt of the right of the Trustee in Bankruptcy to take advantage of the failure to refile properly. See *Lockhart* v. *Garden City Bank & Trust Co.,* 2 Cir., 116 F.2d 658, 662 and cases there cited." 119 F.2d 605, 607.

By the decision below in the instant case, the Trustee was not allowed to "take advantage" of the improper refiling (of the Continuation Statement) by Respondent Princeton, notwithstanding that there was no record of Appellant's claimed security interest on the date of filing the Petition for Rearrangement.

Besides the conflict among the various Circuits, which the Petitioner submits that this Honorable Court should resolve, the Writ of Certiorari should further be granted:

> ". . . because the issue is important in the administration of the Bankruptcy Laws, and is one of first impression in this Court." *Reading* v. *Brown,* 391 U.S. 471, 475 (1968).

Simply stated, the issue is whether or not purported equitable principles alone can be used to defeat the Trustee's rights and powers under Sec. 70(c) of the Bankruptcy Act (11 U.S.C. 110(c)). It is the Petitioner's position that the holding of the Court below, based solely on "equities", rather than the law as written by Congress, could have a profound effect on the administration of the Bankruptcy laws in that Trustees' rights pursuant to Sec. 70(c) of the Act will now be held subject to claimed security interests which a search of the filing records

would not disclose as of the time of the filing of the Petition in Bankruptcy. The legislative history of Sec. 70(c) is quite clear as to the powers Congress sought to give a Trustee under the *Chandler Act of 1938.* As pointed out in Colliers:

> Section 70(c) of the Act as revised by the Act of 1938 contained provisions that prior thereto were not contained in Sec. 70 at all. Further revision in 1950, 1952 and 1966 was intended to achieve simplification and clarification of the provisions and a strengthening of the position of the trustees. . . . The second sentence [of §70 (c)] purports to confer certain statuses upon the trustee as of the date of bankruptcy . . . the status of a judgment creditor, the status of a creditor who obtained an execution returned unsatisfied, and the status of a creditor then holding a lien by legal or equitable proceedings as to all property upon which a creditor of the Bankrupt could have obtained such a lien at bankruptcy. Since 1950 it has been immaterial for the purpose of this second sentence whether or not the property has come into the possession or control of the Court." 4A *Colliers,* Sec. 70.45, pp. 557-8.

See generally 4A *Colliers on Bankruptcy,* Sec. 70.45, 70.46, 70.47, pp. 557-583, for a thorough discussion of the legislative history of Section 70(c) of the Bankruptcy Act.

The basic meaning of Section 70(c) is that the Trustee's rights and powers, vis a vis, any creditors claiming a secured interest are determined as of the date of bankruptcy. The decision of the Third Circuit here would subject the Trustee to rights of a creditor which rights

existed *before* but *not on* the crucial date of filing. See *Lewis* v. *Manufacturers National Bank,* 364 U. S. 603 (1961) wherein it was held, *inter alia,* that the rights of a Trustee are determined as of the date of filing.

As stated by Justice Douglas in *Lewis*:

> "We think that one consistent theory underlines the several versions of Section 70(c), which we have set forth, *vis,* that the rights of creditors—whether they are existing or hypothetical—to which the Trustee succeeds are to be ascertained as of the 'date of bankruptcy' not at an anterior point of time. That is to say, the Trustee acquires the status of a creditor as of the time when the Petition in Bankruptcy is filed. We read the statutory words 'the rights of a creditor (existing or hypothetical), then holding a lien' to refer that date." 364 U.S. at 607.

Both the District Court and the Bankruptcy Court below, made a determination that the claimed security interest of Respondent Princeton was unperfected at the time of the filing of the Petition under Chapter XI of the Bankruptcy Act by virtue of Princeton having filed its Uniform Commercial Code Continuation Statement some twenty-one (21) months prior to the period prescribed by the Uniform Commercial Code, N.J.S.A. 12A:9-403(3).

The Third Circuit felt that the Continuation Statement probably should have been filed within the six (6) month period immediately prior to the expiration of the Financing Statement, but they failed to make the ultimate decision to that effect:

> "While we find much of Appellee's argument for a 'mandatory' construction persuasive, we do not find it necessary to decide the question."

Thus, even though the Court indicated that the Respondent's security interest was unperfected, their ultimate decision resulted in giving Princeton a perfected security interest in the collateral.

It must be emphasized that this decision was based solely upon the "equities" the Third Circuit found existing against the New Jersey Secretary of State's Office and somehow imputed to the Trustee so as to bar the Trustee's Sec. 70(c) powers.

In *In Re Luther,* 465 F.2d 19 (9th Cir. 1972), it was stated that:

> "Equity, therefore, cannot intervene on behalf of a creditor who has failed to perfect her security as local law demands." 465 F. 2d 19, 21.

Also to the point regarding equitable consideration is *Prisbey* v. *Noble,* 505 F.2d 170 (10th Cir. 1974), which dealt with Sections 60(b) and 67(d)(g) of the Bankruptcy Act, the Court stated:

> "Equitable considerations do not allow a court to set aside the applicable bankruptcy law and to order preferential payments. *In Re American Fuel & Power Co.,* 151 F. 2d 470 (6th Cir. 1945). The preservation provisions of 11 U.S.C. Sec. 96(b) and 107(d)(g) allow preservation for the benefit of the estate and not specific creditors." 505 F.2d 170, 177.

The Third Circuit has obviously set aside the applicable bankruptcy law through the use of the "equities". This is not only in conflict with *Luther, supra* and *Prisbey, supra,* but it flies in the face of the historical development of Section 70(c), which has been amended over the years

in order to expand the rights of the Trustee in Bankruptcy. See *Lewis* v. *Manufacturers National Bank, supra;* 1950 *U.S. Code Congressional Service,* page 1985; 1966 *U.S. Code Congressional and Administrative News,* page 2022; 4A *Collier on Bankruptcy* §70.47.

CONCLUSION

This case involves substantial questions of Bankruptcy law. The effective administration of the Bankruptcy Act will be greatly and adversely affected by allowing so-called equitable considerations to be asserted against the Receiver/Trustee; considerations which are totally contrary to the applicable statutory law passed by Congress.

As a result of the Opinion of the Third Circuit, the rights and powers of the Receiver/Trustee under Section 70(c) of the Bankruptcy Act have been severely handicapped and in order to resolve this issue of law and policy, and to resolve the conflict between the Circuits as to the Trustee's rights *vis a vis* unperfected security interests, this case should be reviewed by this Court.

For these and other reasons stated, this Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

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APPENDIX A

Opinion of the United States Court of Appeals for the Third Circuit

(Filed—July 8, 1976)

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 75-2197

In the Matter of:

CALLAHAN MOTORS, INC., a corporation of the State of New Jersey,

Debtor,

PRINCETON BANK AND TRUST COMPANY,

Appellant.

APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY
(No. B-233-73 IN BANKRUPTCY)

Argued April 8, 1976

Before GIBBONS, Circuit Judge, CLARK*, *Associate Justice*
HUNTER, *Circuit Judge*

* Sitting by designation.

Kleinberg, Moroney, Masterson & Schachter
Robert S. Molnar
Attorneys for Callahan Motors, Inc.

Smith, Stratton, Wise & Heher
Garrett M. Heher
Ann Reichelderfer
Attorneys for Princeton Bank and Trust Company

HUNTER, *Circuit Judge:*

The dispute involved in this appeal arose in the aftermath of a petition under Chapter XI of the Bankruptcy Act[1] filed by Callahan Motors, Inc. (formerly known as Cregar Motors). Appellant Princeton Bank and Trust Co., which had been involved in the financing of the debtor's automobile dealership, filed a motion to reclaim certain property (funds and automobiles) which it asserted were covered by a financing statement and continuation statement filed under the provisions of Article 9 of the Uniform Commercial Code.[2]

The matter came on for hearing before the Bankruptcy Judge, and the following factual background, not disputed here, was developed.

Appellant filed its financing statement in March 1965. This statement, which was derived from a security ar-

[1] 11 U.S.C.A. § 701 *et seq.*

[2] It is undisputed that New Jersey is the source of relevant state law. The Uniform Commercial Code became effective in New Jersey on January 1, 1963, as Subtitle 1 of N.J.S.A. 12A. The section of the Code dealing with the expiration of financing statements and the filing of continuation statements is N.J.S.A. 12A:9-403, pertinent portions of which are set forth in the text.

rangement in the nature of trust receipt agreements, complied in all respects with the requirements of the UCC. Since the financing statement did not state a shorter duration, it was effective for 5 years, and, absent an effective continuation statement, would expire in March, 1970.[3] On or about July 1, 1967, the Department of State of New Jersey sent the following letter to all banks:[4]

IMPORTANT NOTICE TO SECURED PARTIES OF FINANCING STATEMENTS FILED UNDER UNIFORM COMMERCIAL CODE

12A:9-403.

(2) A filed financing statement which states a maturity date of the obligation secured of 5 years or less is effective until such maturity date and thereafter for a period of 60 days. *Any other filed financing statement is effective for a period of 5 years from the date of filing.* The effectiveness of a filed financing statement lapses on the expiration of such 60 day period after a stated maturity date or on the expiration of such 5 year period, as the case may be, unless a continuation statement is filed prior to the lapse. Upon such lapse the security interest becomes unperfected. A filed financing statement which states that the obligation secured is payable on demand is effective for 5 years from the date of filing.

[3] N.J.S.A. 12A:9-403(2).

[4] Affidavit of H. McGrory, supervisor of the Uniform Commercial Code Section of the Department of State. Appendix, p. 26A.

(3) A continuation statement may be filed by the secured party (i) within 6 months before and 60 days after a stated maturity date of 5 years or less, and (ii) otherwise within 6 months prior to the expiration of the 5 year period specified in subsection (2) Any such continuation statement must be signed by the security party, identify the original statement by file number and state that the original statement is still effective. Upon timely filing of the continuation statement, the effectiveness of the original statement is continued for 5 years after the last date to which the filing was effective whereupon it lapses in the same manner as provided in subsection (2) unless another continuation statement is filed prior to such lapse. Succeeding continuation statements may be filed in the same manner to continue the effectiveness of the original statement.

To remain effective, Continuation Statements must be filed for all Financing Statements filed January 2, 1963 and thereafter. This office will accept Continuation Statements beginning July 1, 1967.

PLEASE FILE EARLY.

There was no evidence that appellant ever received the letter,[5] but counsel for appellant stated that "we probably received it." (App. p. 46a).

[5] The only arguably relevant testimony was that of P. Harkness, an Assistant Vice President of Princeton Bank and Trust Co. He testified that he was not familiar with any of the notices issued by the Secretary of State with regard to the filing of Financing State-

(Footnote continued on following page)

On December 29, 1967, appellant filed a continuation statement on the appropriate form,[6] referring by number for the filing of March 5, 1965. The Secretary of State accepted the filing fee and delivered to appellant an acknowledgment copy evidencing the filing of the continuation statement. This action was in accordance with the usual practice of the Secretary at that time.

In January, 1968, however, this practice changed. From that date on, the Secretary of State's office returned unfiled to secured parties those continuation statements deemed "premature," namely those submitted more than six months prior to the expiration date of the financing statement, with a form explanation. Appellant never received any notification that its continuation statement was deemed premature, although it had been filed 27 months prior to the expiration date of the financing statement.

In March, 1971, the Secretary removed from the file and destroyed both appellant's original financing statement (by then expired) and the continuation statement

(Footnote continued from preceding page)

ments under the Uniform Commercial Code. In view of Mr. Harkness' testimony that he had not had occasion to file financing statements or continuation statements as part of his duties, his lack of familiarity with the letter in question is of doubtful significance. See p. 6-7a.

[6] The form submitted was actually a multi-purpose form on which appellant checked boxes marked "Continuation" and "Other." The notation under "Other" concerned a change of address of the secured party. That the Secretary of State recognized this form as having two purposes is demonstrated by the fact that *two* \$3.00 filing fees are marked "Pd." on the acknowledgment copy. See p. 23A.

(deemed premature). No notice of this action was given to appellant.

The debtor experienced financial difficulties of increasing severity, sold automobiles covered by the security agreement with appellant "out of trust," and ultimately filed its Chapter XI petition in February, 1973. Appellee Sterns was appointed receiver.[7]

The Bankruptcy Judge denied the motion to reclaim property in May, 1973.[8] The district court denied a petition for review, holding that the pertinent provisions of the UCC require that a continuation statement be filed within the last six months before the expiration of the financing statement and that appellant's continuation statement was therefore premature and ineffective to extend the perfected security interest beyond March, 1970. The district court also rejected appellant's argument that even if the security interest was thus unperfected, it was nevertheless prior to the trustee's claim.[9] *In Re Callahan Motors,* 396 F.Supp. 785 (D. N.J. 1975).

[7] The debtor was adjudicated a bankrupt on December 30, 1974, while this matter was pending in the district court.

[8] The Bankruptcy Judge did enter an order directing the receiver to maintain in an interest-bearing account proceeds of the sale of vehicles claimed by appellant, pending review in the district court. This order was continued by the district court pending the disposition of this appeal.

[9] This argument raises questions of the viability of the doctrine of *Pacific Finance Corp.* v. *Edwards,* 304 F.2d 224 (9th Cir. 1962), in this Circuit, and the applicability of that doctrine to the present facts. In view of our disposition of this case, we have no occasion to express any opinion on these issues.

On this appeal, Princeton Bank and Trust first contends that the district court erred in construing the reference in N.J.S.A. 12A:9-403(3) to the six month period immediately prior to the expiration of a financing statement as mandatory. Appellant stresses the language "[a] continuation statement may be filed . . . within 6 months prior to the expiration. . . ." and argues that a continuation statement *may* also be filed at any other time before expiration of the financing statement. Apparently there are no reported cases resolving this question; the trustee has cited two opinions of state attorneys general (Ohio and Iowa)[10] taking the "mandatory" position, i.e., that continuation statements filed more than six months before expiration are ineffective.

We need not detail the arguments from policy and rules of statutory construction which have been advanced by the parties and the court below. While we find much of the appellee's argument for a "mandatory" construction persuasive, we do not find it necessary to decide the question.

Appellant argues that even if the district court's interpretation of § 9-403(3) is correct as a general rule, that rule cannot apply here. Appellant relies on § 9-403(1) and *In re Royal Electrotype Corp.,* 485 F.2d 394 (3d Cir. 1973).[11] § 9-403(3) provides that

[10] These are reported at 14 UCC Rep. Serv. 860 (1974), and 12 UCC Rep. Serv. 1251 (1973), respectively.

[11] *Royal Electrotype* involved Pennsylvania law, but we may assume without deciding that the same result would obtain under the analogous provisions of New Jersey law. See note 12, *infra.*

> Presentation for filing of a financing statement, tender of the filing fee and acceptance of the statement by the filing officer constitutes filing under this chapter.

The *Royal Electrotype* court held that a creditor was entitled to reclaim property even though a filing officer had misfiled a financing statement by reversing the names of the secured party and the debtor. The court relied on official UCC Comment 1 under § 9-407 (this comment also appears in the New Jersey version):

> Note, however, that under Section 9-403(1) the secured party does not bear the risk that the filing officer will not properly perform his duties: under that Section the secured party has complied with the filing requirements when he presents his financing statement for filing and the filing fee has been tendered or the statement accepted by the filing officer.

This Comment, determined by the *Royal Electrotype* court to be a correct statement of state law,[12] fully justifies the

[12] The court relied on indications that the Pennsylvania courts were "giving full force and effect to . . . the official comments accompanying the text." 485 F.2d at 397. Although such indications are perhaps less distinct in regard to New Jersey courts, we note that the comments have been cited, e.g. *Southern New Jersey Airways, Inc.* v. *National Bank of Secaucus,* 108 N.J. Super. 369, 261 A.2d 399 (App. Div. 1970); *A.J. Armstrong, Inc.* v. *Janburt Embroidery Corp.,* 97 N.J. Super. 246, 234 A.2d 737 (Law Div. 1967), and we believe that the comments are at least some indication of New Jersey law.

result in that case. Its applicability to the present case, however, is less certain, since it is not immediately clear that a continuation statement is a "financing statement" within the meaning of § 9-403(1), or that events constituting "filing" constitute the "timely filing" required by § 9-403(3).

We need not, however, go so far as to adopt a general rule that acceptance of a continuation statement by a filing officer cures an untimely presentation. The present record discloses not just a simple acceptance of appellant's statement and fees, but a course of conduct by the Secretary of State which caused the asserted imperfection in filing almost as certainly as did the clerical error in *Royal Electrotype.* On these particular facts, we believe that the same result as in *Royal Electrotype* should follow.

Our consideration of the Secretary's conduct arguably should begin with the July, 1967 letter. The trustee argues that this letter served to put appellant on notice of the "proper" time for filing continuation statements. Even if we were to conclude that appellant should be found to have received this letter,[13] we could not agree with the trustee's analysis of its import. The first two paragraphs merely quote the statutory language. The concluding four lines could just as easily be interpreted as advising that continuation statements "for all Financing Statements filed January 2, 1963 *and thereafter*" (emphasis added) could and should be filed as soon after July 1, 1967 as conveni-

[13] Under New Jersey law, there is a presumption that mail properly addressed, stamped and mailed was received by the party to whom it was addressed. *National State Bank* v. *Terminal Construction Corp.,* 217 F.Supp. 341, 355 (D. N.J. 1963), *aff'd* 328 F.2d 315 (3d Cir. 1964) (per curiam).

ent. Thus it may be that the July, 1967 letter, if received by appellant, triggered the filing which is now attacked as premature.[14]

Whatever the effect of the letter, it appears that the Secretary's handling of appellant's December, 1967 submission caused the non-compliance, if any, with the UCC provisions. The Secretary, though deeming the continuation statement premature,[15] not only failed to convey this interpretation to appellant but, by accepting the filing fee and returning an acknowledgment of filing, acted affirmatively to give appellant every reason to believe that it was in compliance with all applicable state requirements. It seems certain enough that if the Secretary had followed his post-1967 policy of returning "premature" continuation statements unfiled, with an explanation, in dealing with appellant's submission, the latter would have

[14] Appellee argues that the fact that the letter was sent four and one-half years after the effective date of the UCC is significant. This fact does indeed suggest that the Secretary viewed the six-month period as mandatory, but it alone cannot be said to have put appellant on notice of this viewpoint, in view of the language discussed in the text, indicating that continuation statements should be filed even for those financing statements filed after January 2, 1963.

[15] Appellant also argues that the Secretary's pre-1968 practice of "accepting" continuation statements filed more than six months before the expiration of the financing statement constituted an administrative interpretation of the statute which should lead this court to adopt a "permissive only" view of the six-month period. We find that the record far more strongly supports the conclusion that the Secretary at all times considered such filings "premature." See, e.g., p. 28a, and note 14, *supra*.

filed a continuation statement during the six months prior to the March, 1970 expiration date.[16]

The prejudice to appellant was compounded when the Secretary in 1971 removed and destroyed appellant's financing and continuation statements without notifying appellant. Once again it seems entirely reasonable to suppose that if appellant had been informed of the Secretary's interpretation of the statute and consequent treatment of its filings, appellant would have promptly re-filed. Even though Princeton Bank's security interest had, in the view of the Secretary, become unperfected at this point, such a refiling would have been effective against the trustee in this proceeding.

In sum, we decline to decide whether, under New Jersey law, a continuation statement is timely if filed more than 6 months before the expiration of a financing statement or should always be deemed timely if accepted by the filing officer; we hold only that on these particular facts, a resolution of these questions so as to bar appellant's motion to reclaim would be inconsistent with the equitable character of bankruptcy proceedings. See *Bank of Marin* v. *England,* 385 U.S. 99 (1966); *Pepper* v. *Litton,* 308 U.S. 295 (1939).

[16] Our characterization of the Secretary's conduct as improper and misleading is supported by the Opinion of the Attorney General of Ohio, discussed in text at note 10:

> I would recommend, however, that notice be given to those whose filings were accepted even though they were not timely. Such persons believe their filings to be effective and should be notified of their actual status.

14 UCC Rep. Serv. at 873.

Appendix A

The judgment of the district court will be reversed and the proceedings remanded with a direction of a further remand to the referee to grant appellant's petition for reclamation to the extent justified by the financing and continuation statements.

To the Clerk:

Please file the foregoing opinion.

James Hunter, III, Circuit Judge

APPENDIX B

Judgment of the United States Court of Appeals for the Third Circuit

UNITED STATES DISTRICT COURT

For the Third Circuit

No. 75-2197

In the Matter of:

Callahan Motors, Inc., a corporation of the State of New Jersey,

Debtor,

Princeton Bank and Trust Company,

Appellant.

(D.C. No. B-233-73 in Bankruptcy)

On Appeal from the United States District Court For the District of New Jersey

---

Present: Gibbons, *Circuit Judge*, Clark,* *Associate Justice*, and Hunter, *Circuit Judge*.

This cause came on to be heard on the record from the United States District Court for the District of New Jersey and was argued by counsel.

* Sitting by designation.

Appendix B

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the said District Court, filed August 18, 1975, be, and the same is hereby reversed and the proceedings are remanded with a direction of further remand to the referee to grant appellant's petition for reclamation to the extent justified by the financing and continuation statements. Costs taxed against appellee.

Attest:

THOMAS F. QUINN
Clerk

July 8, 1976

APPENDIX C

Opinion of the United States District Court for the District of New Jersey

In the Matter of CALLAHAN MOTORS, INC., a corporation of the State of New Jersey, Debtor.

No. B 233-73.

United States District Court,
D. New Jersey.

Bankruptcy Division.

June 18, 1975.

A creditor sought review of a bankruptcy proceeding in which its application to reclaim automobiles and sale proceeds from the bankrupt debtor was denied. The District Court, Clarkson S. Fisher, J., held that a New Jersey statute, a Uniform Commercial Code section, providing that a continuation statement to extend the period of security interest may be filed within six months before expiration of the five-year period requires filing within the six months' period, and an earlier filing is premature and ineffective. Under a New Jersey statute providing that presentation for filing of a financing statement, tender of filing fee and acceptance of statement by filing officer constitute filing, the premature filing of the continuation statement was not effective, in view of the creditor's error, though the office of the New Jersey Secretary of State ac-

cepted the continuation statement without hesitation and without advising the secured party that if the statement was deemed premature it would have no effect and would be destroyed along with the original financing statement upon the natural expiration date. A bankruptcy receiver takes on the status of "ideal" or "perfect creditor" regardless of whether there were any creditors who had or did not have knowledge of unperfected security interest.

Petition denied.

1. SECURED TRANSACTIONS 98

New Jersey statute, a Uniform Commercial Code section, providing that continuation statement to extend period of security interest may be filed within six months before expiration of five-year period requires filing within the six months' period, and earlier filing is premature and ineffective. N.J.S.A. 12A:1-102, 12A:9-403(3).

2. SECURED TRANSACTIONS 98

In New Jersey statute, a Uniform Commercial Code section, providing that continuation statement to extend period of security interest may be filed within six months before expiration of five-year period and providing that succeeding continuation statements may be filed in the same manner to continue effectiveness of original statement, phrase "the same manner" refers to time limit imposed in initial sentence of section as well as to other requirements set forth for filing of continuation statement. N.J.S.A. 12A:1-102, 12A:9-403(3).

See publication Words and Phrases for other judicial instructions and definitions.

3. SECURED TRANSACTIONS 98

Under New Jersey statute providing that presentation for filing of financing statement, tender of filing fee and acceptance of statement by filing officer constitute filing, premature filing of continuation statement was not effective, in view of creditor's error, though office of New Jersey Secretary of State accepted continuation statement without hesitation and without advising secured party that if statement was deemed premature it would have no effect and would be destroyed along with original financing statement upon natural expiration date. N.J.S.A. 12A:9-403 (1, 3).

4. OFFICERS 103

Public officers cannot bind government by acts outside their express authority.

5. SECURED TRANSACTIONS 98

Where creditor admitted having received notice from Secretary of State of New Jersey that Secretary would begin accepting continuation statements for filing as of July 1, 1697, 4½ years after Uniform Commercial Code became effective in New Jersey, this should have sufficed to put creditor on notice that continuation statements filed less than 4½ years after original financing statement would be ineffective. N.J.S.A. 12A:9-403 (1, 3).

6. BANKRUPTCY 205

Bankruptcy receiver takes on status of "ideal" or "perfect creditor" regardless of whether there were any credi-

tors who had or did not have knowledge of unperfected security interest. N.J.S.A. 12A:9-301; Bankr.Act, §§ 70, sub. c, 301 et seq., 11 U.S.C.A. §§ 110(c), 701 et seq.

7. Bankruptcy 205

Under Bankruptcy Act, creditors actual knowledge of unperfected security interest has no bearing on rights of receiver, N.J.S.A. 12A:9-301(1); Bankr. Act, § 70, sub. c, 11 U.S.C.A. § 110(c).

8. Bankruptcy 205

State statute such as New Jersey statute concerning status of unperfected security interest cannot serve to deprive bankruptcy receiver of his federally created status of lien creditor without notice. N.J.S.A. 12A:9-301(1); Bnkr. Act § 70, sub. c, 11 U.S.C.A. § 110(c).

Markowitz & Zindler, Trenton, N. J., for debtor.

Joel H. Sterns, Sterns & Greenberg, Trenton, N. J., receiver in bankruptcy.

Kleinberg, Moroney, Masterson & Schachter by Robert Molnar, Newark, N. J. for Receiver.

Smith, Stratton, Wise & Heher by Garrett M. Heher, Princeton, N. J., for Princeton Bank and Trust Co. Frank Petrino on the brief.

Opinion

Clarkson S. Fisher, District Judge.

This is a petition for review by the Princeton Bank and Trust Company (hereinafter Bank) of a bankruptcy proceeding in which its application to reclaim automobiles and sale proceeds from the bankrupt debtor was denied.

On February 23, 1973, the debtor in this action, Callahan Motors, Inc., (hereinafter Callahan) filed a Chapter XI Petition in bankruptcy. An Order was entered appointing Joel H. Sterns, Esquire, as Receiver. Callahan was engaged in the business of selling automobiles to retail customers and had, prior to the filing of the Chapter XI Petition, financed its purchases of automobiles for resale with the petitioner Bank by use of trust receipts. Pursuant to the agreement between the Bank and Callahan, the Bank would pay the wholesaler the cost of these vehicles and Callahan would then execute a promissory note and trust receipt security agreement covering the cost of these vehicles. When each vehicle was sold, Callahan was obligated to repay the Bank the amount loaned by the Bank for the cost of the purchase of the vehicle, with interest at 7½% per year.

Although the debtor was required by the terms of the trust receipt security agreement to keep the sale proceeds of each vehicle separate with payment to the Bank to be made immediately on the amount due on each vehicle, it was discovered upon a check of the debtor's inventory subsequent to the filing of the Chapter XI Petition, that 29 vehicles had been sold "out of trust" by Callahan without reimbursement to the Bank, resulting in a delinquency of $83,896.31 for the vehicles sold "out of trust."

Further, the Bank filed a Notice of Motion to reclaim the 73 vehicles purchased by the debtor with funds advanced by the Bank which were still in the debtor's inventory, amounting to $112,853.25. Therefore, the Bank's total claim against the debtor for monies loaned on the trust receipts financing agreements amounted to $196,-749.56.

The Bankruptcy Judge, on April 24, 1973, approved a Consent Order directing the receiver to hold the proceeds from the sale of any such vehicle in escrow, or the vehicles themselves, pending final disposition by this Court of the issues raised in the Bank's Petition for Review of the Bankruptcy Court's decision with respect to its Motion to Reclaim.

The motion is based on the following:

On March 5, 1965, the Bank filed a financing statement with the Secretary of State perfecting its security interest in Callahan's inventory of new and used cars and the proceeds of the sale on other disposition of said inventory. On December 29, 1967, the Bank filed a continuation statement along with the appropriate filing fee and was given a copy of the statement stamped "filed" by the Office of the Secretary of State. The Bank was never informed that the continuation statement would "be deemed ineffective by the Office of the Secretary of State and no record [would be] made thereof," nor that the Secretary of State would destroy the Bank's financing statement one year after its expiration date even though it had accepted the continuation statement for filing and had not rejected it as being premature. (Affidavit of Helen McGary, Supervisor of UCC Section of Department of State, March 28, 1973). The original financing statement was, in fact,

destroyed along with the continuation statement as the Secretary of State determined that the latter did not result in expanding the term of the original financing statement beyond the five-year period which expired in March of 1970.

Yet on January 1, 1968, only a few days after the Bank's continuation statement was filed, the Secretary of State's Office adopted a policy of returning unfiled to secured parties any documents which were deemed to be presented for filing prematurely with a rejection form appropriately marked.

On May 2, 1973, the Bankruptcy Judge entered on Order denying the Bank's application to reclaim the automobiles and the proceeds of the sale based on the Court's determination that the continuation statement filed in late 1967 had no validity and did not extend the period of the original financial statement from 1970 to 1975 so as to render the continuation statement effective as of the filing of the Chapter XI Petition in 1973.

The Bank then filed a Petition for Review which cited two reasons for reversing the order denying reclamation:

1. The Bank's claim was secured prior to the rights of the Receiver because of the filing of the continuation statement by the petitioner with the Secretary of State of New Jersey on December 29, 1967, which extended the effective date of the filing of the original financial statement from March, 1970 to March, 1975.

2. Even if the above is not found to be so, the unperfected security interest of the Bank is prior to any interest of the receiver, pursuant to N.J.S.A. 12A:9-301.

Thus, the first issue to be determined is whether the filing of the continuation statement and its acceptance by the Secretary of State's Office in December, 1967 continued the effective date of the original statement from March, 1970 to March, 1975. The applicable statute is as follows:

> N.J.S.A. 12A:9-403
>
> "(2) . . . Any other filed financing statement (one which does not have a stated maturity date) is effective for a period of 5 years from the date of filing. The effectiveness of a filed financing statement lapses . . . on the expiration of such 5-year period, . . ., unless a continuation statement is filed prior to the lapse. Upon such lapse the security interest becomes unperfected.
>
> (3) A continuation statement may be filed by the secured party . . . (ii) otherwise within 6 months prior to the expiration of the 5-year period specified in subsection (2). Any such continuation statement must be signed by the secured party, identify the original statement by file number and state that the original statement is still effective. Upon *timely* filing of the continuation statement, the effectiveness of the original statement is continued for 5 years after the last date to which the filing was effective whereupon it lapses in the same manner as provided in subsection (2) unless another continuation statement is filed prior to such lapse." (emphasis added).

Petitioner contends that the wording of the statute is that while a continuation statement "may be filed" within six months prior to the expiration of the five-year period,

such filing within that period of time is not mandatory, but merely directory. Respondent urges, however, that the continuation statement, if filed at all, must be filed during the six-month period immediately prior to the expiration date of the original financing statement. In support of this assertion, the Bankruptcy Judge reasoned that: (1) "It is a cardinal principal of statutory interpretation that full effect should be given, if possible, to *every* word of a statute." (2) ". . . it has been well settled for more than a century that filing requirements of this type (N.J.S.A. 12A:9-403(3)) will be strictly enforced." (3) Under predecessor statutes (e. g. Chattel Mortgage Act), premature filing voided the security interest.

[1] There seems to be a paucity of authority construing this and like statutes. However, it would seem clear that N.J.S.A. 12A:9-403(3) requires a *timely* filing and indicates the filing period is six months prior to expiration of the five-year period.

Nevertheless, petitioner submits that contrary to the Bankruptcy Judge's opinion, the filing requirements need not be adhered to strictly. The Uniform Commercial Code (UCC) specifically provides that:

> "[t]his Act shall be liberally construed and applied to promote its underlying purposes and policies." N.J.S.A. 12A:1-102.

However, it cannot be thought that in applying a liberal construction of the UCC, clear and unambiguous language should be overlooked to defeat requirements of timely filing imposed by 12A:9-403(3). This, in itself, would lead to absurd results in that it would provide for tacking, a result which impliedly is sought to be avoided precisely by the timeliness standard established in the statute.

"If the words of a statute are affirmative and absolute, and show that no discretion was intended to be given those delegated the task of making the statute operate, than the words of the statute must be given effect peremptorily. Only when construing a statute where an ambiguity exists, or a literal interpretation may lead to absurd results, may there be resort to the principle that the spirit of the law controls the letter. *Giordano* v. *City Commission of City of Newark,* 2 N.J. 585, 594, 67 A.2d 454 (1949). Presently the court is faced with neither an ambiguous statute nor a statute which creates absurdities; moreover, the letter amplifies the spirit." *Mulligan* v. *New Brunswick,* 83 N.J.Super. 185, 191, 199 A.2d 82, 85 (Law Div. 1964).

The Court finds, therefore, that N.J.S.A. 12A:9-403(3) presents, in clear and unambiguous language, the standard which must be followed in filing a continuation statement. There exists no ambiguity in the word "may" as such word refers to whether or not a continuation statement is, in fact, filed. It has no reference to the prescribed six-month period in which to file. Further indication of this intent may be found in the final sentence of 12A:9-403(3), which states as follows:

> "Succeeding continuation statements may be filed in the same manner to continue the effectiveness of the original statement."

[2] The phrase "the same manner" must necessarily refer to the time limit imposed in the initial sentence of the section as well as to other requirements set forth for filing of the continuation statement (e. g. signed by the secured party, etc.).

[3] Petitioner contends, however, that assuming, *arguendo,* that the Bank submitted its continuation statement to the Secretary of State prematurely, it was still filed on December 29, 1967 with the Office, pursuant to the express language of N.J.S.A. 12A:9-403(1), which states as follows:

> "Presentation for filing of a financing statement, tender of the filing fee and acceptance of the statement by the filing officer constitutes filing under this chapter."

There is no dispute that the Bank conformed with these requirements for filing. Further, there is no doubt that the Office of the Secretary of State accepted the continuation statement without hesitation and *without* advising the secured party that if the statement was deemed premature, it would have no effect and would be destroyed along with the original financing statement upon its natural expiration date. Therefore, petitioner asks this Court to find that the continuation statement was valid in that it was accepted by the Secretary of State's Office.

In so urging, the Bank relies on *In Matter of Royal Electrotype Corporation,* 485 F.2d 394 (3d Cir. 1973). In that case, the Secretary of State of Pennsylvania accepted for filing a security agreement but in indexing the agreement, indexed the debtor as the creditor and the creditor as the debtor, with the result that a search of the records against the actual debtor would not have disclosed the filed security agreement. The Third Circuit Court of Appeals held, in reversing the District Court, that the secured party does not bear the risk that the filing officer will improperly perform his duties and that under Pennsylvania law, the creditor's interest was perfected as soon

as the financing statement was presented and accepted, and the filing fee tendered.

> "Cases from other jurisdictions have consistently held that the secured party does not bear the risk of improper indexing by the filing officer *so long as the secured party has not by his own conduct caused the error.*" Id. at 397. (emphasis added).

The Court concedes that when a creditor fulfills his obligations with regard to filing and in spite of this, a mistake results due to an error by the Office of the Secretary of State, then clearly the creditor should not be penalized. However, although the action or inaction by the Secretary of State here is unfortunate in that it failed to notify the Bank that its continuation statement was filed prematurely and further it failed to inform the Bank in March, 1971, that the continuation statement was not effective to extend the original financing statement, with the resultant destruction of both documents, these steps were consequences of the petitioner's erroneous filing of the continuation statement almost two years prior to the prescribed period set forth in N.J.S.A. 12A:9-403(3).

[4] A continuation statement must be timely filed to continue the effectiveness of the original filed financing statement. If the requirement of timely filing is not met, there results a lapse, as public officers cannot bind the government by acts outside their express authority.

[5] I must conclude that the acceptance of the continuation statement by the Secretary of State for filing cannot render it effective to support the Bank's petition for reclamation. To further support this conclusion, it should be noted that Princeton admits having received notice

from the Secretary of State that the Secretary would begin accepting continuation statements for filing as of July 1, 1967 ($4\frac{1}{2}$ years after the UCC became effective in New Jersey). This should have sufficed to put petitioner on notice that continuation statements filed less than $4\frac{1}{2}$ years after the original financing statement would be ineffective.

The final point urged by petitioner is that even if the Bank's security interest is not perfected under the UCC, its unperfected security interest is still prior to any interest of the receiver in bankruptcy. This claim is based on N..S.A. 12A:9-301, which states, in pertinent part as follows:

> "(1) Except as otherwise provided in subsection (2), an unperfected security interest is subordinate to the rights of . . .
>
> (b) a person who becomes a lien creditor without knowledge of the security interests and before it is perfected;
>
> • • •
>
> (3) A 'lien creditor' means a creditor who has acquired a lien on the property involved by attachment, levy or the like and includes an assignee for the benefit of creditors from the time of assignment, and a trustee in bankruptcy from the date of the filing of the petition or a receiver in equity from the time of appointment. *Unless all the creditors represented had knowledge of the security interests such a representative of creditors is a lien creditor without knowledge even though he personally has knowledge of the security interest.* (emphasis added).

In construing the above provisions with those of Section 70(c) of the Bankruptcy Act, 11 U.S.C.A. Section 110(c), it is urged by petitioner that the Receiver only stands in the shoes of an actual creditor who extended credit during the period of time a security interest was unperfected, not a hypothetical or ideal creditor. However, under Section 70(c), the Receiver, as of the date of bankruptcy, shall have the rights and powers of:

> "(3) A creditor who upon the date of bankruptcy obtained a lien by legal or equitable proceedings upon all property, whether or not coming into possession or control of the court, upon which a creditor of the bankrupt upon a simple contract could have obtained such a lien, *whether or not such a creditor exists.* (emphasis added).

[6] Therefore, the Receiver takes on the status of an "ideal" or "perfect creditor" regardless of whether there were any creditors who had or did not have knowledge of the unperfected security interest. "That section (70(c)) confers on the trustee in bankruptcy the status of an ideal hypothetical creditor and as such gives him the status of a creditor without notice, despite any actual knowledge he may personally have had at the time of bankruptcy and regardless of the fact that there may not exist any actual creditor without notice." *In Matter of Babcock Box Co.,* 200 F.Supp. 80 (D.Mass.1961). See also *Taplinger* v. *Northwestern National Bank,* 101 F.2d 274 (3d Cir. 1938); *In re Lindsey,* 131 F.Supp. 11 (D.N.J. 1955).

[7] Accordingly, the receiver is accorded "ideal" status as the perfect creditor who has complied with all require-

ments necessary under the applicable law for a lien by legal or equitable process. He has such status irrespective of whether there are actually any such creditors in existence as his status is derived not by the nature of the creditors of the estate, but by the Bankruptcy Act itself. *4A Collier on Bankruptcy,* Section 70.53 at p. 636 (14th ed.).

Thus, the assertion by petitioner that in order for the receiver to maintain an action under Section 70(c), he must demonstrate that actual creditors exist who did not have knowledge of the Bank's unperfected security interest is erroneous. Reliance on *Pacific Finance Corporation* v. *Edwards,* 304 F.2d 224 (9th Cir. 1962) is misplaced, as although it does support this contention, the holding is clearly contrary to the overwhelming weight of authority and has been severely criticized. See *4A Collier,* Section 70.50, pp. 611-614.

Proof that all creditors did have knowledge of the unperfected security interest, which the Bank has not even attempted to establish, would nevertheless not suffice to impute this knowledge to the receiver and effect his rights under the strong-arm clause of Section 70(c). Therefore, "there is no necessity for demonstrating that he does or does not represent at least one actual creditor without notice." *4A Collier,* Section 70.53, pp. 636-7.

[8] In conclusion, it is apparent that a state statute, such as N.J.S.A. 12A:9-301(1), cannot serve to deprive the receiver of his federally created status as a lien creditor without notice. As previously stated, the actual knowledge of all the creditors has no bearing on the rights of the receiver under Section 70(c). Therefore, the Uniform Commercial Code cannot be deemed to affect this position.

Accordingly, the Bank's unperfected security interest does not have priority over the rights of the receiver in bankruptcy.

Thus, the petition of the Princeton Bank and Trust Company is denied.

Submit an order.

APPENDIX D

Bankruptcy Court Decision by Bankruptcy Judge Amel Stark

UNITED STATES DISTRICT COURT
DISTRICT OF NEW JERSEY

In Proceedings for an Arrangement Under Chapter XI of the Bankruptcy Act

Docket No. B-233-73

On Petition for Review by Princeton Bank and Trust Company

CERTIFICATE OF REVIEW

In the Matter of:

CALLAHAN MOTORS, INC., a corporation of the State of New Jersey,

Debtor.

To: The Honorable Judges of the United States District Court For The District of New Jersey:

I, Amel Stark, one of the Referees in Bankruptcy of the United States District Court, District of New Jersey, to whom the above entitled estate has been referred, do hereby certify the record as follows:

That on the 2nd day of May, 1973, an Order denying the Application of Princeton Bank and Trust Company to reclaim property was entered in these proceedings.

That the said Princeton Bank and Trust Company, feeling aggrieved by the entry of this Order, has petitioned for review thereof, and

That the question presented by this review is whether or not the referee erred in denying the aforesaid Application To Reclaim.

The Petition For Review filed by the Princeton Bank and Trust Company recites as the basis for the Petition as follows:

> "1. The claim of Petitioner Princeton Bank and Trust Company was a secured claim prior to the rights of the Receiver because of the filing of the Continuation Statement by the Petitioner with the Secretary of State of New Jersey on December 29, 1967, which extended the effective date of the filing of the original Financing Statement from March of 1970 to March of 1975.
>
> "If the filing of the Continuation Statement by Petitioner with the Secretary of State of New Jersey on December 29, 1967, did not extend the effective date of the original Financing Statement from March of 1970 to March of 1975, the unperfected security interest of the Petitioner, Princeton Bank and Trust Company will still be prior to any interest of the Receiver because of the provisions of R. S. 12A:9-301."

Findings of Fact

1. This case was commenced by the filing of a Petition under Chapter XI of the Bankruptcy Act on February 22, 1973, and the matter is still pending in this court.

2. Joel H. Sterns, Esquire, was appointed as Receiver on February 22, 1973, and duly qualified by filing the required bond.

3. Notice of Motion To Reclaim Property was filed on behalf of Princeton Bank and Trust Company on March 14, 1973, and was scheduled for hearing on April 4, 1973 before the Referee.

4. Application to reclaim property attached to the aforesaid Notice of Motion recites as follows:

> (a) That at the time of the filing of the Petition for an Arrangement Under Chapter XI herein, the Debtor had in its possession certain automobiles, which automobiles were purchased by the debtor for resale with moneys advanced by the Petitioner Bank pursuant to Trust Receipt Security Agreement and Demand Promissory Note, executed by the Debtor at the time the moneys were advanced by Bank for the purchase of each vehicle.
>
> (b) That the Trust Receipt Security Agreements provided:
>
> > "In the event of a breach of any of the terms hereof or trustee's bankruptcy, insolvency or receivership, Bank may declare the note (if same is not payable on demand) accompanying the Trust Receipt, or any renewal thereof, imme-

diately due and payable. Should Trustee fail to pay the said note when due, Bank is hereby authorized to enter upon any premises at any time with or without legal process or notice to take possession of said chattels or the proceeds thereof."

(c) That as a result of the filing of the Petition Under Chapter XI, Bank became entitled, pursuant to the Trust Receipt Security Agreement, to immediate possession of all of the automobiles covered by said agreements as well as to the amounts received by the Receiver from the sale of motor vehicles.

5. The Debtor is in the retail automobile business, and until the filing of the Chapter XI Petition, had engaged in floor-plan financing of its automobiles with the Applicant Bank.

6. Applicant Bank claims to have perfected a valid prior lien on the basis of a Financing Statement filed with the Secretary of State of New Jersey, Uniform Commercial Code Section, on March 5, 1965, listing Cregar Motors, Inc. as Debtor. Cregar Motors, Inc. is the predecessor of the Debtor in the within action.

7. Although the original Financing Statement would have expired by operation of State law on March 5, 1970, Applicant Bank claims to have continued the effectiveness of the original Financing Statement for five years from its expiration, that is, until March 5, 1975, by virtue of a "Continuation Statement" filed on December 29, 1967.

8. Applicant Bank contends further that even if its security interest is unperfected, it is not subordinate to the Receiver and the creditors represented by the Receiver.

9. Applicant Bank finally contends that any lien of the Receiver is not enforceable against the motor vehicles and sale proceeds involved in its financing because they are merely held in trust for the Bank.

10. The only question that could possibly be raised with respect to the filing of the continuation statement is that it was filed *prior to* six months before the expiration of the five year period of the original Financing Statement.

11. It is the practice in the Office of the Secretary of State of New Jersey, Uniform Commercial Code Section, to clear its records of all Financing Statements upon the expiration date, or at the end of five years, if there is no expiration date, after searching for continuation statements filed within six months of the termination date or within six months of the end of five years, if there is no expiration date.

12. A search of the records in the Office of the Secretary of State of New Jersey, ordered by the Receiver, and received by him on March 28, 1973, does not show the Applicant Bank as a secured party.

Conclusions of Law

N.J.S.A. 12A:9-403(3) provides:

"A continuation statement may be filed by a secured party (i) within six months before and 60 days after

> a stated maturity date of 5 years or less and (ii) *otherwise within 6 months prior to expiration of the 5 year period specified in subsection (2).* (emphasis mine). Any such continuation statement must be signed by the secured party, identifying the original statement by file number and state that the original statement is still effective. Upon timely filing of the continuation statement, the effectiveness of the original statement is continued for 5 years after the last date to which the filing was effective whereupon it lapses in the same manner as provided in subsection (2) unless another continuation statement is filed prior to such lapse. Succeeding continuation statements may be filed in the same manner to continue the effectiveness of the original statement."

Since the Continuation Statement was not filed *within* 6 months prior to the expiration of the 5 year period specified in subsection (2) the Financing Statement lost its force and effectiveness on March 5, 1970.

It is a cardinal principal of statutory interpretation that full effect should be given, if possible, to *every* (emphasis mine) word of a statute (2 Sutherland, Statutory Construction, Paragraph 4705 (Third Edition 1943)). This principal was most recently restated by the New Jersey Supreme Court in *Gabin* v. *Skyline Cabana Club,* 54 N. J. 551 (1969). In the pertinent part of the opinion, a unanimous Court held at page 555 of that Opinion, that the Legislature would not have included a phrase if it had not intended that phrase to have meaning. The Court stated:

> "It is a cardinal rule of statutory construction that full effect should be given if possible, to every word of a statute. We cannot assume that the Legislature used meaningless language."

In *Handleman* v. *Marwin Stores Corp.,* 53 N. J. 404 (1969) the New Jersey Supreme Court held that it could not, in interpreting an action of the Legislature, assume that the Legislature was making an empty gesture.

The question raised in this Petition for Review is a novel one, and there are no known decisions construing the pertinent statutory provision (N.J.S.A. 12A:9-304(3). This is so, since it has been well settled for more than a century that filing requirements of this type will be strictly enforced.

A leading authority on secured transactions states:

> "9UCC Section 9-403(3) allows the filing of a continuation statement within six months prior to the lapse of the original financing statement. The continuation is good for another five years, and successive continuations can be similarly made. By comparison, the ordinary effectiveness under U. S. C. A., Section 11, is three years, and the extensions are for only one year. Under U. T. R. A., Section 13, the corresponding periods are both one year . . ." *Peter P. Coogan, Public Notice Under The Uniform Commercial Code And Other Recent Chattel-Security Laws, Including "Notice Filing"* Secured Transactions Under U. C. C., Section 604 (13) New York; Mathew Bender, F. M. 9, Page 496.

While there are no decisions on this particular U. C. C. provision, there are repeated cases involving the question

of premature filing under predecessor Statutes. *Annotation, Premature Refiling of Chattel Mortgages*, 63 A. L. R. 591 (1929).

Judge Learned Hand, in *In re Frederick Steffens,* 31 F 2d 660, 661 (1927) stated:

> "We have already held that the failure to refile a chattel mortgage within the year made it void, and we think it equally encumbent upon the mortgagee not to file it prematurely . . . the statute makes its own terms which no creditors need go beyond. If he finds the mortgage on file, he need search only for thirty days before the succeeding year expires."

In New Jersey, the basis for this decision has been laid in numerous cases going back to 1869. *National Bank of the Metropolis* v. *Sprague et als.,* 20 N. J. Eg. 13 (Chancery Division, 1869).

In *Heinselt* v. *Smith,* 34 N. J. L. 215 (Supreme Court of New Jersey, 1870) the Court found that in order to give a chattel mortgage continuing effect beyond the year from its original filing, the copy, with the required statement, must be filed *within* (emphasis mine) 30 days preceding the expiration of the year *and not any sooner* (emphasis mine).

In *Ferris* v. *Chambers,* 51 Colo. 368, 117 P. 994 (1911) the Statute in question, as in the instant matter, used the word *may*:

> "The lien of any chattel mortgage given to secure the payment of any indebtedness which has been duly admitted to record as provided by law *may* within thirty days after the maturity of the last installment . . . be extended . . ."

After a lengthy discussion of statutory interpretation, the Colorado Supreme Court stated:

> "The inevitable conclusion from all the foregoing considerations is that the Legislature had in mind the thirty days after maturity for the filing of the statement. This being so, the statement in this case was prematurely filed for the period after maturity did not commence until the beginning of the next day."

Even if the Secretary of State of New Jersey admitted acceptance of the continuation statement of Applicant Bank for filing, the weight of authority indicates that this would not be sufficient to determine the effect thereof:

> "Under the liberal provisions of the Code, the filing officer is under a duty to accept any copy of an instrument, regardless of how it is filed, where the instrument is not obviously defective upon its face, leaving the effect thereof to be judicially determined." 1962 *Opinion of the New Mexico Attorney General* #62-126, October 9, reported in 1 U. C. C. R. S. 748."

In *In Re Smith* (D. C. Penna. 205 F. Supp. 27 (1962) the Court said:

> "If a financing statement does not substantially comply with the statutory requirements, U. C. C. Section 4-401(2) is not operative even though the statement has been accepted for filing within the county, where neither the debtor's trustee in bankruptcy nor his creditors had knowledge of such filing."

The purpose of Article 9 of the Uniform Commercial Code is to give notice to all who proposed to deal with the the debtor and who are diligent enough to search out his dealings with other creditors.

The underlying basis for the statute and the effectuation thereof, was restated in the 1972 comments to Section 9-403, reported under the heading, *1972 Revision of Article Nine* in the U. C. C. R. S. at U. C. C. Appendix, Page 93:

> "The theory of this Article is that the public files of financing statements are self-clearing, because the filing officer may automatically discard each financing statement after a period of five years plus the year after lapse required by subsection (3) unless a continuation statement is filed, or the financing statement is still effective under subsection (6). This theory materially lessens the tension that would otherwise exist to have the files cleared by termination statements under Section 9-404. Similarly, a person searching the files need not go back past this five years plus one year; and if the indices are arranged by years, he has a limited and defined search problem. The section asks the filing officer to attach financing statements whose life has been continued by continuation statements to the latter statements, so that anything contained in the files of old years can be discarded."

Having failed to perfect its Security Interest, Applicant Bank has no priority over the Receiver and the creditors represented by the Receiver.

In *In Re Luckenbill* (D. C. Penna. 156 F. Supp. 129 (1957)) the Court stated:

> "A trustee in bankruptcy may challenge the perfection of a security interest on the ground that it has not been properly filed even though there is no creditor under state law who has standing to do so."

In Beneficial Finance Company v. *Kurland, Inc.,* 293 N. Y. 2d 647 (1968) the Court stated:

> "It is clear beyond doubt that the Debtor's Trustee in Bankruptcy prevails over the reclamation petition of a secured creditor where the unsecured creditor failed to perfect his interest by a proper filing."

Further, *In re Babcock Company,* D. C. Mass. 200 F. Supp. 80 (1961) concluded that:

> "The fact that the Trustee in Bankruptcy individually has active knowledge of the unperfected interest does not bar him as Trustee in Bankruptcy from claiming priority over the unperfected interest, because he has the right of an ideal creditor and would only be barred if all the creditors had knowledge of the unperfected interest."

In Re Smith (supra) makes it plain that the extra burden is upon the Applicant Bank to establish that the creditors or the Receiver had notice of the claimed lien, for the Court stated:

> "If there has not been a proper filing but the creditor claims that he should nevertheless prevail over others because they had knowledge of the contents of the statement which was filed, the burden is upon the creditor to establish that they had such knowledge, and conversely, the burden is not upon

the Debtor's Trustee in Bankruptcy to establish that he did not have such knowledge."

The Trust Receipt Security Agreement is merely a financing arrangement and does not create a true trust situation.

In *In Re Black Watch Farms, Inc.*, U. S. D. C., S. D. N. Y., April 22, 1971, Bankruptcy Docket No. 70 B 691, reported in Uniform Commercial Code Reporting Service, at Page 151, the Court stated:

"A bank which has made advances to the debtor and which held promissory notes made by 'herd owners' (persons purchasing breeding cattle from the debtor and contemporaneously contracting with the debtor for the care, feeding and breeding of their herds) payable to the debtor who pledged the notes to the bank and assigned to it the debtor's possessory lien covering the cattle of six of the herd owners, the debtor undertaking to retain possession of the cattle as agent for the assignee, did not have a valid perfected security interest in the cattle of the six heard owners which was superior to the rights of the receiver appointed for the debtor in proceedings under Chapter XI of the Bankruptcy Act. The Bank has not filed financing statements to perfect its security interests and had never had physical possession of the collateral. Its claim of perfection by possession by reason of assignment to it of the debtor's 'possessory lien' covering the six herds of cattle pursuant to which the cattle were retained in debtor's possession as agent for the assignee was without merit since the debtor could not act as the secured party's agent for purposes of perfection by possession."

I hand up herewith for the information of the Court, the following papers:

1. *Exhibit No. 1 for Review*—Application and Notice of Motion To Reclaim Property By Princeton Bank and Trust Company
2. *Exhibit No. 2 for Review*—Order dated May 2, 1973, denying Reclamation Application of Princeton Bank and Trust Company
3. *Exhibit No. 3 for Review*—Copy of Certificate of Search, Uniform Commercial Code Section of the Secretary of State of New Jersey Number S 120 597 dated March 28, 1973, covering Callahan Motors, Inc.
4. *Exhibit No. 4 for Review*—Copy of Certificate of Search, Uniform Commercial Code Section of the Secretary of State of New Jersey Number S 120 598, dated March 28, 1973, covering Cregar Motors.
5. *Exhibit No. 5 for Review*—Copy of Form Letter (U. C. C. #30) entitled "Important Notice to Secured Parties of Financing Statements Filed Under Uniform Commercial Code" from Department of State, State of New Jersey.
6. *Exhibit No. 6 for Review*—Affidavit of Helen McGrory, Supervisor of Uniform Commercial Code Section of Department of State, dated March 28, 1973.
7. *Exhibit No. 7 for Review*—Supplemental Affiadit of Helen McGrory, dated April 19, 1973.

Appendix D

8. *Exhibit No. 8 for Review*—Copy of Petition To Review Referee's Order .

All of which is respectfully submitted.

Amel Stark
Referee in Bankruptcy

Dated at Trenton, New Jersey
this 17th day of July 1973

APPENDIX E

Order Granting Motion Extending the Filing of the Petition for Rehearing

UNITED STATES COURT OF APPEALS

for the Third Circuit

July 21, 1976

No. 75-2197

In the Matter of

Callahan Motors, Inc., a corporation of the State of New Jersey,

Debtor,

Princeton Bank and Trust Company,

Appellant.

(D.C. No. B-233-73 In Bankruptcy)

Present:

Hunter, *Circuit Judge.*

1. Motion by appellee, Joel H. Sterns, Receiver and Trustee in Bankruptcy for Callahan Motors, Inc., for an extension of time within which to file a petition for rehearing pursuant to Rule 40, F.R.A.P., from its present due date of July 22, 1976, to and including August 6, 1976, together with affidavit in

support of said motion attached hereto, in the above-entitled case. The opinion was filed and the judgment entered on July 8, 1976.

Respectfully,

T. F. QUINN
Clerk

enc.
ags

The foregoing Motion is granted.

By the Court,
JAMES HUNTER, III
Judge

Dated: July 29, 1976

APPENDIX F

Order of the United States Court of Appeals Denying Petition for Rehearing

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

No. 75-2197

PRINCETON BANK AND TRUST COMPANY,
Appellant,

v.

JOEL H. STERNS, TRUSTEE IN BANKRUPTCY FOR CALLAHAN MOTORS, INC.,
Appellee.

SUR PETITION FOR REHEARING

Present: GIBBONS, *Circuit Judge*, CLARK,* *Associate Justice*, and HUNTER, *Circuit Judge*

The petition for rehearing filed by Appellee in the above entitled case having been submitted to the judges who participated in the decision of this court and no judge who concurred in the decision having asked for rehearing, the petition for rehearing is denied.

JAMES HUNTER, III, Judge

Dated Aug 18 1976

* Sitting by designation.